



PUBLIC EMPLOYEE RETIREMENT SYSTEM OF IDAHO
607 North 8th Street
BOISE, IDAHO 83702

MINUTES
OF
MEETING OF RETIREMENT BOARD

The Board of the Public Employee Retirement System of Idaho met at the PERSI Administration Building, 607 North Eighth Street in Boise, Idaho at 8:32 a.m., February 25, 2003. The following members were present:

Jody B. Olson
Susan K. Simmons
Pamela I. Ahrens
Dennis L. Johnson

J. Kirk Sullivan was absent and excused. Trustee Susan K. Simmons joined the meeting at 9:10 a.m., having been excused to attend to other state agency business. The electronic projection of materials and documents discussed in the meeting was handled by Carol Peterson. Executive Director Alan H. Winkle, Deputy Attorney General Brad Goodsell, Financial Officer James Monroe, Chief Investment Officer Robert Maynard, and Management Assistant Joanne C. Ax were also in attendance. Other persons attending portions of the meeting were:

Rod MacKinnon
Bill Palumbo
Drew Black
Brian McGrath
Dennis Fitzpatrick
Cody Barney
Chris Growney
Mike Boren
Wendy Young
Phil Suess

Mountain Pacific Investment Advisors
Mountain Pacific Investment Advisors
DB Fitzpatrick & Co.
DB Fitzpatrick & Co
DB Fitzpatrick & Co
DB Fitzpatrick & Co
Clearwater Advisors
Clearwater Advisors
Mercer
Mercer

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|-------------------|-----------------------|
| Lucinda Smith | Mellon |
| Bill Kincaid | Mellon |
| John McCarrick | Mellon |
| Brent Nye | Boise School District |
| Charlie Brown | REAI |
| Robert Schmidt | Milliman USA |
| Jim Coleman | PERC Retired Teachers |
| Cecile McMonigle | PERSI |
| Rhonda Yadon | PERSI |
| Richelle Sugiyama | PERSI |
| John R. Doner | PERSI |

OLD BUSINESS

Commendation: Chairman Olson read a letter he received from members of the Endowment Fund Investment Board thanking Investment Officer Richelle Sugiyama and CIO Robert Maynard for their assistance during the past six months. The letter stated that "their efforts led to significant improvements in efficiency, processes, and investment performance." The letter was signed by Nick Hallett, Gavin Gee, Dean Buffington, Representative Bill Deal, Senator Dean Cameron, Thomas Kealey, William D. Mitchell, Parker Woodall and John Taylor. Chairman Olson added the thanks of the Board for this effort, noting that considerable volunteer time was involved.

Approval of the Minutes: By motion duly made by Trustee Ahrens and seconded by Trustee Johnson, the Board unanimously approved the minutes of the January 28, 2003, regular meeting of the Retirement Board as submitted.

PORTFOLIO

Disclosure: CIO Robert Maynard provided the Board with a list of investment related or local outside activities in which he is engaged. These included a list of Boards on which he serves as well as those entities to which he has recently or is currently providing pro bono investment advice.

Mellon Quarterly Report: Lucinda Smith introduced her manager, John McCarrick, from their Everett, Massachusetts office. He gave a brief update and background on Mellon Financial Services.

Mr. Maynard reviewed the Russell/ Mellon Fourth quarter 2002 report which had previously been furnished to the Board. He noted that the PERSI fund is defensively positioned – when the markets go down, PERSI outperforms the indices. When markets go up, peer rankings drop because of their underlying asset allocation; PERSI underperforms because of the

defensive posturing. We need a 70% allocation to equities in order to provide COLA's and meet our other liabilities.

Chairman Olson commented that about a year ago at our Investment Manager Conference, the consensus was that international equity markets would outperform domestic markets. Mr. Maynard said that we are still waiting for that to happen. Trustee Ahrens asked about the effect of current events on international markets. Mr. Maynard said unless there is a severe disruption of oil, he does not expect the current impending war situation to drastically affect international markets. Oil supplies are relatively secure, inventories are built up and covered by cross agreements. If it should follow the trends seen in the Gulf War, markets would decline at the beginning, then return to their trend. A different situation could occur, depending on events in such a conflict. Mr. Maynard had e-mailed various "what if" scenario's from a recent conference to the Trustees and said that exercise gives a good overview of expected economic impacts of various situations. Because of the uncertainty, no sustained market rise is expected until war begins.

He completed his review of the Russell Mellon report by discussing manager style universe rankings, percentile rankings. In general, these rankings reflect the implementation of our policy. Our policy is our long-term navigation tool and is not going to change. If there is a sudden market rise, we will still under perform our benchmarks, but look great against our peers.

Monthly Portfolio Update Mr. Maynard discussed his investment report dated February 23, 2003, which he had updated from the one previously furnished to the Board. In the report and in his discussion, Mr. Maynard noted the following:

Since the last Board meeting, the fund is almost exactly even (up 0.1%). War jitters and general uncertainty have generally been driving the market, with no real change in either economic or earnings expectations. The market also appears to be at the bottom range of its large roller-coaster movements it has exhibited over the past couple of years.

All managers are either within their expected characteristics or have reasonable explanations for slight deviations. All managers are also performing as expected vs. their respective benchmarks. The TIPs account has the best absolute performance, while international and small cap equities have the worst. Zesiger and Genesis have the best relative performance for the fiscal year to date, while Brandes and Scudder have the worst. The portfolio as a whole continues to exhibit its primarily defensive character

that it developed late last year. This means that if the market turns around quickly, our relative performance will lag for a while.

Mr. Maynard's report stated the current value of the fund as of February 23, 2003 was \$5,884,511,642. The fiscal year-to-date return percentage is negative 7.0% and the month-to-date return was a negative 0.1%.

Manager Comments: The Chairman invited managers who were present to comment on the markets and the economy. Brian McGrath expects a stronger economy by the end of the year with higher interest rates, and has therefore taken a short duration position in the portfolio. Locally, he expects even more layoffs at Micron by the end of the year unless things change. Chairman Olson asked what the average compensation of 1300 Micron employees would be. No one had an answer. Clearwater Advisors expects rates to stay low and predicts rates may dip even further in the short-term. By year-end, they agree that rates will be higher, but not by more than expected, and as such, are not as short on duration. Geo politics – the Philippines, Korea, and Colombia, in addition to Iraq, are concerns. Bill Palumbo noted that a common view of investors is that the markets will go up once the war is completed or starts and the military outcome becomes clear. He does not believe most investors are positioned for that. Once the outcome of war becomes clear, he expects a huge surge in interest in the markets. Mercer's perspective is that once we are past the war, we will still have choppy times.

Chairman Olson said he is serving on a national task force studying the corporate governance issue.

CHOICE PLAN:

Defined Contribution Overview: Executive Director Winkle provided historical information on the Choice Plan. The plan began when existing state 401(k) plans were transferred to PERSI for administration. They were then expanded to include PERSI members. Gain Sharing added accounts for most PERSI members and the plan was changed to its present design.

Wendy Young of Mercer Investment Consulting discussed their concerns with manager ING. Since several people have left this firm, their management style has changed. Mercer recommends a search for a replacement for this investment manager. Ms. Young said that the Bush Administration's proposals for retirement savings are sending a strong message to Americans that they must be personally responsible for retirement income. Several dramatic proposals have been made. Ms. Young expects dramatic changes in how retirement is funded in the future.

Phil Seuss had previously provided copies of his presentation to the Board. He said PERSI members have invested more than \$88 million in the

Choice plan. The plan is structured to give participants access to the various sectors of the market and a choice between active and passive management. The funds also focus on managers who take a core approach rather than pursuing a value, growth or other style of investing.

Mr. Suess reiterated that because of recent management changes and the investment style changes since we hired ING as a Choice Plan fund, he recommends a search for their replacement. There are 834 participants with about \$2 million invested in this fund. In response to a question from the Chair, Mr. Suess indicated a search for a new manager would cost about \$10,000. Trustees delayed making a decision on that issue. Mr. Winkle said we will investigate this further and see if we have a similar fund on the DB side and provide more information to the Board.

Choice Plan Mellon Report : Bill Kincaid had previously provided copies of the Management Report to the Trustees. He reviewed the allocations of participants to the various funds. 77% of the Choice Plan total is invested in the PERSI Total Return Fund. Those who are contributing voluntarily to the plan have about 57% of their funds in the PERSI Total Return Fund. Currently, the SEI Stable Value fund has the second-highest percentage at 10% of the voluntary contributions. More than \$88 million is currently invested for participants in funds of their choice. Answering a question from the Chair, Mr. Winkle said several cities, counties and schools added employer gain sharing dollars to their employee's gain sharing accounts. Six or seven employers have an on-going match for their employees.

8% of eligible PERSI members are deferring part of their salary to the plan, an increase of 3% from last year. DC Plan Specialist Gay Lynn Bath said rollovers into the fund are accepted and that feature is being used.

Mr. Kincaid reviewed the fees including record keeping fees paid by participants and PERSI. Mr. Winkle said that when gain sharing occurred, the Board decided to furnish the vehicles and support out of the total fund. If members want to use the active managers, they pay those investment fees.

Participants who terminate and leave their funds in the plan must begin paying their own fees. Three funds offer rebates: Dodge and Cox, Brandes and Dreyfus. Those rebates are sent to the trust, then back to the participants. While not significant in dollars, they are significant in basis points. Trustee Johnson asked if these fees were the average for managing \$88 million in a 401(k). Mr. Winkle said when we started this fund, we knew that the administration costs would be fixed and seem high at the beginning. As the fund matures and we see an increase in participation and total dollar amount managed, the percentage will be more comparable to other funds. Investment fees as a percent of assets are the important fees to monitor. Mr. Kincaid said an updated website and calculator will be on the internet by the end of the summer with more features for our members.

Choice Plan Statistics: DC Plan Specialist Gay Lynn Bath reviewed the basic statistics of the plan including calls from members, rollovers, distributions, in-service transfers which are used to buy back service in the base plan, and internet and IVR use. She reported 28,789 web inquiries in 2002. In December 2002, there were 100 new participants in the Choice Plan bringing the total number of member's contribution as of December 31, 2002 to 5186. That is a 21% increase from the previous year. Our pre-retirement seminars raise awareness of the plan and encourage members to use this vehicle as they plan for retirement. Participants can use the modeling calculator on the website or talk with a counselor without a charge. Ms. Bath briefly discussed the Bush Administration's proposal that would consolidate various retirement savings accounts, provide lifetime savings accounts and revise the traditional IRA's. She said experts contend that as written, it is doubtful these proposals will be accepted. Initial industry reaction is not favorable.

FISCAL:

Update and Expense Reports: Financial Officer James Monroe told the Board that an upgrade to EASYPAY, a system for electronically transmitting contributions to PERSI was rolled out this month, allowing web access for initiating transactions. The Request for Proposals for our annual audit is nearly ready for release. Trustee Simmons has reviewed and commented on the draft RFP. This will be an agreement for the fiscal year 2003 with renewal options for the subsequent four years. With Bob Maynard's approval, the sick leave fund is being rebalanced at the end of February since it currently has a 5% variance from the target asset allocation of 60% equity and 40% fixed income. Mr. Monroe reviewed the Administrative and Portfolio expense reports for the month ended January 31, 2003, which had previously been furnished to the Board. Trustee Simmons asked for details on encumbrance dollars; Mr. Monroe will provide them to her.

Financial Statements – Senior Accountant Rhonda Yadon reviewed the financial statements for the quarter ended December 30, 2002. There was nothing unusual in the report. The audit is completed and the Annual Report is printed.

MEMBERSHIP

Disability Program Update: Membership Manager Judy Aitken and her assistant, Judy Shock, provided data regarding the PERSI disability program. The increase in applications and the need for added expertise in the approval and denial process led to hiring a third party administrator for the program over a year ago. Charts showing disabilities by applicant age, diagnosis, by employers, length of service and region of the state provided details from 1999 through 2002. If PERSI members are disabled on the job, Worker's

Compensation is the primary insurer and we become the secondary insurer.

Chairman Olson asked if the PERSI disability benefit was unusually rich compared to other systems. Mr. Winkle said the benefit itself is high and the requirements to qualify are also high compared to other systems. The actuary calculates .49% of pay out of 13.65% total contribution rate is allocated for disability retirement, which is not a big expense item actuarially.

Trustee Ahrens said claims in insurance are mirroring the trends shown in Ms. Aitken's report. Answering a question from Trustee Johnson, Ms. Ahrens said in her department a risk group meets on a regular basis to review claims and injuries. Mr. Winkle said the state workforce is about 10 years older than the private workforce with an average age of 45, which may account for part of the increase in disability applications.

LEGAL

Final Decision and Order – Deputy Attorney General Brad Goodsell said Roy Applewhite had appealed the denial of his disability retirement. A hearing was held before a hearing officer on December 17, 2002 and a recommended decision was issued January 17, 2003. The recommended order affirms the final decision denying his application for disability retirement benefits. By motion duly made by Trustee Johnson, seconded by Trustee Simmons and unanimously approved, the Board issued a FINAL DECISION AND ORDER adopting the recommended decision of the hearing officer in the contested case of: In the matter of the disability retirement application of Roy Applewhite, Case No. CC-02-02.

Ethics Discussion – Mr. Goodsell reviewed the main provisions of Idaho Code concerning ethics in government, including 1) prohibitions against contracts with officers, 2) the Ethics in Government Act, and 3) the Bribery and Corrupt Influence Act. He suggested two easy-to-remember "safe harbors" to use when determining if a third party may pay for something for a state employee or public official:

1. If the expense could be reimbursed by the state as a legitimate business expense (i.e. travel to a conference, hotel,), payment by a third party is acceptable.
2. The "\$50 Rule," which limits the value of an item (something the state would not otherwise pay for) to \$50.

He expects additional guidance from the Attorney General's office about what other safe harbors there might be. Trustees may contact Mr. Goodsell with specific questions that might arise.

EXECUTIVE DIRECTOR

New Employer: By motion duly made by Trustee Johnson, seconded by Trustee Ahrens and unanimously approved, the Board welcomed The

Fremont County District Library in Ashton, Idaho as a new PERSI employer effective February 1, 2003.

Status Update: Executive Director Winkle reviewed the summary of PERSI projects report that had previously been provided to the Board. The PERSI budget will be set on February 24 and is a Maintenance of Current Operations budget. The actuarial review audit is progressing as is the member survey RFP. At the March Board meeting Clearwater Research will present survey information and solicit input from the Board. RFP's are being prepared for a Process Review Project and Call Management/IVR study.

Legislative Review: Each Friday, Mr. Winkle provides an update to the Trustees and interested parties on bills that could affect PERSI. He reviewed the current status of those.

Personnel Matters: Chairman Olson said Idaho Code Section 67-23455(b) permits the Board to hold an executive session to discuss matters exempt from disclosure (i.e. matters concerning personnel matters). Due to the fact that matters of these types were before the Board, he submitted to the Board for consideration the necessity of holding an executive session. By motion duly made by Trustee Johnson seconded by Trustee Simmons and unanimously approved, the Board convened in executive session at 11:15 a.m.

At 11:30 a.m., the Board reconvened in regular session. Chairman Olson said during the executive session, the trustees discussed matters concerning personnel issues and no decisions were made.

FUTURE BOARD MEETINGS

Tuesday, March 18, 2003, 8:30 a.m., Boise - PERSI office

Tuesday, April 22, 2003, 8:30 a.m., Boise - PERSI office

Tuesday, May 20, 2003, 8:30 a.m., Boise - PERSI office

Tuesday, June 17, 2003, 8:30 a.m., Boise - PERSI office - Tentative

Adjournment: There being no further business before the Board, the meeting was adjourned at 11:31 a.m.

Jody B. Olson
Chairman

Alan H. Winkle
Executive Director